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MANUFACTURERS HANOVER

# Financial Digest

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Analysis of Business Trends Plus Selected Financial Indicators

## The Dollar Plunges . . .

The dollar has begun the New Year on a decidedly weaker note, slumping to its lowest level in 6½ years against the German mark and breaching record lows with respect to the Japanese yen. The decline against the yen is particularly noteworthy, since it came despite massive intervention by the Bank of Japan. Yet the foreign exchange markets are clearly unimpressed by such intervention and continue to sell the dollar heavily.

More than anything else, it was the announcement of a record $19.22 billion trade deficit in November which once more undermined confidence in the dollar and sent it tumbling. In particular, the shortfall suggested to many market participants that the U.S. Administration would not be adverse to a further weakening of the dollar in order to rectify the huge trade imbalance. Indeed, such sentiments were validated by the Administration's seeming lack of concern over the dollar's plight, and by its continued refusal to sanction Federal Reserve intervention on behalf of the beleaguered dollar.

A close examination of the dollar's performance suggests that the Administration's attitude is not unfounded. The dollar's steep descent from its lofty peaks of February 1985 will, at some point, help to stimulate exports. However, according to this Bank's trade-weighted dollar index, the dollar's overall decline has not yet been sufficient to narrow substantially our deficit. This is because the steep fall of the dollar against such key currencies as the Japanese yen, German mark and Swiss franc has obscured the fact that it hasn't fallen much against the currencies of a number of other countries with which we are doing a growing volume of business. In addition, in "real" terms, adjusted for inflation, the dollar's decline is even less noticeable.

## . . . But Not Against All Currencies . . .

For example, while the dollar has plunged against the mark and yen during this period, it has, in fact, gained ground against the currencies of such significant trading partners as South Korea and Australia while declining only slightly against the currencies of Taiwan, Singapore and Canada. Therein lies a major reason behind the failure of our overall trade deficit to improve. As a result, any emphasis on the mark and yen as benchmarks of the dollar's performance is highly misleading, since Germany and Japan account for just 17 percent of total U.S. exports. Canada, on the other hand, accounts for a more significant 21 percent share.

Furthermore and perhaps most important is the fact that on an inflation-adjusted basis, the dollar's decline is even less. The MH trade-weighted dollar at midweek (see table)

Manufacturers Hanover Economics Department 17/270

**MANUFACTURERS HANOVER'S TRADE-WEIGHTED DOLLAR**

| Country | Feb. 1985 High: Currency/ U.S. $ | Jan. 28 Actual: Currency/ U.S. $ | Percent Change: Jan. 28 vs. Feb. 85 | Export Price Caused vs. Feb. 85 | Real vs. Feb. 85 |
|---|---|---|---|---|---|
| Canada* | 1.388 | 1.3375 | – 3.6 | 7.2 | – 10.8 |
| Japan | 261.753 | 150.60 | – 42.5 | – 21.2 | – 21.3 |
| Mexico* | 239.230 | 971.50 | 306.1 | 167.3 | 138.8 |
| Germany | 3.398 | 1.7738 | – 47.8 | – 2.7 | – 45.1 |
| United Kingdom | 0.934 | 0.647 | – 30.7 | – 5.5 | – 25.2 |
| Taiwan | 39.280 | 35.11 | – 10.6 | – 3.0 | – 7.6 |
| South Korea | 843.800 | 857.20 | 1.6 | 6.2 | – 4.6 |
| France | 10.387 | 5.9130 | – 43.1 | – 5.3 | – 37.8 |
| Italy | 2115.059 | 1265.75 | – 40.2 | – 4.6 | – 35.6 |
| Hong Kong | 7.804 | 7.7630 | – 0.5 | 3.4 | – 3.9 |
| Netherlands | 3.865 | 2.0040 | – 48.2 | – 19.1 | – 29.1 |
| Brazil* | 3.866 | 15.51 | 301.2 | 332.8 | – 31.6 |
| Venezuela* | 7.500 | 14.50 | 93.3 | 14.8 | 78.5 |
| Australia | 1.409 | 1.517 | 7.6 | – 0.9 | 8.5 |
| Belgium | 68.542 | 36.80 | – 46.3 | – 11.9 | – 34.4 |
| China* | 2.858 | 3.7314 | 30.6 | 5.0 | 25.5 |
| Singapore* | 2.261 | 2.1250 | – 6.0 | – 1.5 | – 4.5 |

*Uses CPI: Others use export price indexes.

Jan. 28 vs. Feb. 85 Percent Change: 0.99 Actual
9.15 Exp. price caused
–8.16 Real

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was off only about eight percent in real terms from its February 1985 high. While the dollar's real value is down substantially against such key European currencies as the mark, it has not declined that much in real terms with respect to the yen, witness our continued swelling trade deficit with Japan. Indeed, this Bank's calculations reveal that the dollar has fallen by only 20 percent against the yen when Japan's much slower rate of inflation is taken into account. As a consequence, the dollar may no longer be overvalued against the yen—but neither is it low enough to make a significant dent in our bilateral trade deficit with Japan, which reached $60 billion last year.

On the other hand, with regard to the mark, the dollar's decline has translated into more of a real drop than with respect to the yen. This is because the U.S. inflation rate has paralleled Germany's more closely than Japan's. As a result, the U.S. dollar is now undervalued against the mark, suggesting that the U.S. should experience a major narrowing of its bilateral deficit with Germany this year.

### . . . Keeping The Trade Deficit Large

However, until the dollar falls further in

## Short Term Paper Outstanding

(Millions of Dollars)

| Time Deposits of $100,000 or more Weekly Reporting Banks | Latest Week | Change Since Week Ago | Change Since Year Ago |
|---|---|---|---|
| Nationwide (1/14/87) | 156,059 | + 972 | – 7,959 |
| New York City (1/21/87) | 36,057 | + 566 | – 678 |
| **Commercial Paper** (1/21/87) | 336,511 | + 2,845 | + 38,459 |

## Bank Loans

(Millions of Dollars)

**Commercial and Industrial Loans**

| Weekly Reporting Large Commercial Banks | Latest Week | Change Since Week Ago | Change Since Year Ago |
|---|---|---|---|
| Nationwide (1/14/87) | 283,341 | – 3,273 | +25,677 |
| New York City (1/21/87) | 64,801 | – 846 | + 5,901 |

**Total Loans and Leases Gross Adjusted**

| | Latest Week | Change Since Week Ago | Change Since Year Ago |
|---|---|---|---|
| Nationwide (1/14/87) | 789,556 | – 4,224 | +59,564 |
| New York City (1/21/87) | 175,010 | + 1,757 | +17,266 |

## Financial Markets

| | Friday 1/30/87 | Change Since Week Ago | Change Since Year Ago |
|---|---|---|---|
| **U.S. Governments, Closing Yields:** | | | |
| 90-Day Bills† | 5.73% | + .21 | – 1.46 |
| 180-Day Bills† | 5.80 | + .26 | – 1.68 |
| Longest Bills† | 5.89 | + .20 | – 1.66 |
| **Recent Issues:** | | | |
| 61/8S 1/31/89 (When Issued) | 6.28 | + .10 | |
| 65/8S 12/31/90 | 6.60 | + .10 | |
| 71/4S 11/15/96 | 7.16 | + .11 | |
| 71/2S 11/15/16 | 7.47 | + .05 | |
| **Municipals:** | | | |
| Bond Buyer–20 Bond Index* (1/29/87) | 6.56% | + .02 | – 1.30 |
| Blue List Total ($ Million) | $1,643 | + $ 173 | +$ 447 |
| 30-Day Visible Supply ($ Million) | $3,292 | + $1,411 | +$2,961 |
| Total | $4,935 | + $1,584 | +$3,408 |
| **Corporates:** | | | |
| Moody's Aa Composite (1/29/87) | 8.84% | + .02 | – 1.60 |
| 30-Day Visible Supply ($ Million) | $2,647 | – $ 180 | +$1,622 |
| **Stocks:** | | | |
| **Dow-Jones Averages:** | | | |
| Industrials | 2,158.04 | + 56.52 | +587.05 |
| Transportation | 874.88 | + 5.69 | +126.42 |
| Utilities | 224.72 | – 0.64 | + 47.81 |
| 65 Stocks | 822.17 | + 13.60 | +189.67 |
| **N.Y.S.E. Composite Index** | 156.11 | + 2.09 | + 33.98 |
| **N.Y.S.E. Avg. Daily Vol. for Week (000's)** | 179,242 | – 33,344 | +32,934 |

*46% Taxable equivalent 12.15%. † Bond equivalent.

## International Rates

| EURODOLLAR DEPOSIT RATES (bid) | Friday 1/30/87 | Week Ago |
|---|---|---|
| Overnight | 6.06% | 5.88% |
| 1 month | 6.06 | 6.00 |
| 3 month | 6.06 | 6.00 |
| 6 month | 6.06 | 6.00 |
| 1 year | 6.13 | 6.06 |

**EURODOLLAR BONDS**

| Average Yield | | |
|---|---|---|
| Medium Term (5 to 7 yrs.) | 7.13% | 7.13% |
| Long Term (7 to 15 yrs.) | 7.93 | 7.93 |

**FOREIGN EXCHANGE SPOT RATES**

| New York Opening (1/30/87) | U.S. $ Equivalent | Currency Per U.S. $ |
|---|---|---|
| Canada | .7460 | 1.3405 |
| France | .1639 | 6.1000 |
| Germany | .5464 | 1.8300 |
| Italy | .0007683 | 1301.50 |
| Japan | .006502 | 153.80 |
| Mexico | .001025 | 975.55 |
| Switzerland | .6431 | 1.5550 |
| U.K. | 1.5215 | .6572 |

| MH TRADE-WEIGHTED DOLLAR* (1/30/87) | Change Since Week Ago | Change Since 2/27/85 |
|---|---|---|
| | +1.0% | –7.6% |

*Adjusted for Inflation

real terms against all and not just some of the currencies of our major trading partners, the trade deficit will remain a significant impediment to economic growth. In this regard, the dollar must decline against the currencies of such newly industrialized countries of Asia as Taiwan and Korea who have become major trading partners of the U.S. and who are running huge bilateral trade surpluses with us. Taiwan, which is our fourth largest source of imports behind Japan, Canada and Germany, is a notable example. Although it has recently allowed its currency to appreciate slowly against the dollar, its $15.6 billion trade surplus in 1986 (third highest in the world behind Japan and Germany) of which $13.5 billion was accounted for by the U.S., suggests that its currency is still well undervalued.

The widening of the trade deficit has weakened the U.S. economy, and most dangerously of all, aggravated protectionist sentiment in Congress. Thus, unless the dollar falls across the board and not just against some currencies, protectionist legislation may be inevitable—with negative consequences for the world economy. ■

## Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

| | Week Ending 1/28/87 | $ Change Since Week Ago | $ Change Since Year Ago |
|---|---|---|---|
| Reserve Bank Credit | | | |
| U.S. Gov't and Agencies Owned Outright & RPs | 211.774 | + 2.535 | +20.728 |
| Loans to Depository Inst. | .979 | + .581 | + .138 |
| Float | 4.303 | + 3.273 | + 3.324 |
| Total Reserve Bank Credit | 234.192 | + 6.711 | +25.834 |
| Treasury Deposits with Federal Reserve Banks | 15.853 | + 7.551 | − .634 |
| Currency in Circulation | 205.945 | − 1.033 | +15.091 |
| Gov't held for Foreign Acct. by F.R. Banks (End-of-Week) | 163.606 | − 1.443 | +36.184 |
| | **1/28/87** | | |
| Member Bank Reserves: | | | |
| Total Reserves Held | 56.709 | − 3.536 | +10.976 |
| Excess (Deficiency) | 1.170 | + .264 | + .249 |
| Net Free Reserves | .708 | + .092 | + .161 |
| **Monetary Aggregates †** | | **% Change Since 3 Months' Ago*** | **Year Ago** |
| M1 (1/19/87) | 732.2 | + 23.6‡ | + 17.8‡ |
| M2 (December '86) | 2,804.5 | + 9.3 | + 9.3 |
| M3 (December '86) | 3,488.1 | + 7.3 | + 9.0 |
| Domestic Nonfinancial Debt (3rd Q'86) | 7,410.3 | + 11.4 | + 13.5 |

†Seasonally adjusted.

* Seasonally adjusted annual rate.
‡ Four-week moving average.

## New York Money Market

| Offering Rates 1/30/87 | 3 Months | 6 Months | 1 Year |
|---|---|---|---|
| ‡U.S. Treasury Bills | 5.52% | 5.53% | 5.53% |
| * Federal Agencies | 5.70 | 5.65 | 5.65 |
| * Municipal Notes—High Grade (46% Taxable Equivalent) | 7.40 | 6.67 | 7.41 |
| Negotiable Time CDs Manufacturers Hanover | Rates By Arrangement | | |
| * Secondary Market—Prime | 5.90 | 5.90 | 6.00 |

‡Finance Company Paper—Prime

| | |
|---|---|
| 5- 14 days | 5.95% |
| 15- 29 days | 5.93 |
| 30- 59 days | 5.93 |
| 60- 89 days | 5.90 |
| 90-179 days | 5.85 |
| 180-239 days | 5.75 |
| 240-270 days | 5.75 |

‡* Bankers' Acceptances

| | |
|---|---|
| Feb. | 5.90% |
| Mar. | 5.84 |
| Apr. | 5.80 |
| May | 5.72 |
| Jun. | 5.70 |
| Jul. | 5.68 |

‡Industrial Paper—Prime

| | |
|---|---|
| 30- 89 days | 5.93% |
| 90-120 days | 5.85 |

†Federal Funds Effective Rate 6.23%

‡Discount basis. *Subject to availability. † Estimated.

## Selected Business Indicators

(All Dollar Figures in Billions)

| | Latest Period or End of Period | | Previous Period | Year Ago Period |
|---|---|---|---|---|
| Gross National Product (Current Dollars)* | 4th Q'86n | $ 4,268 | $ 4,241 | $ 4,088 |
| Gross National Product (1982 Dollars)* | 4th Q'86n | $ 3,702 | $ 3,686 | $ 3,622 |
| Percent Change, Annual Rate | 4th Q'86n | 1.7 | 2.8 | 2.1 |
| Change in Consumer Prices* | Dec '86n | 2.4% | 3.6% | 4.8% |
| Change in Producer Prices* | Dec '86 | 0.0% | 2.4% | 7.2% |
| Civilian Employment (Thousands of Persons) † | Dec '86 | 110,637 | 110,432 | 108,149 |
| Unemployment as % of Civilian Labor Force † | Dec '86 | 6.7% | 6.9% | 7.0% |
| Personal Income* | Dec '86n | $ 3,555 | $ 3,527r | $ 3,418 |
| Leading Indicators Composite Index (1967=100)† | Nov '86 | 182.5 | 180.4 | 171.6 |
| Industrial Production Index (1977=100) † | Dec '86 | 126.6 | 126.0 | 125.6 |
| Net Change in Consumer Installment Credit † | Nov '86 | $ 4.02 | $ 7.21 | $ 5.64 |
| U.S. Merchandise Trade Balance | Dec '86n | −$ 10.66 | −$ 15.44r | −$ 14.22 |
| Plant and Equipment Expenditures* | 1st Q'87 | $386.82(a) | $394.34(a) | $377.94 |
| Private Housing Starts (Thousands of Units)* | Dec '86n | 1,802 | 1,585r | 1,882 |
| New Construction Expenditures* | Nov '86 | $ 377.0 | $ 379.7 | $ 357.6 |
| Total Business Inventories † | Nov '86 | $ 590.6 | $ 591.6 | $ 582.7 |
| Total Business Sales † | Nov '86 | $ 437.1 | $ 435.8 | $ 431.0 |

*Seasonally adjusted annual rate. Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.

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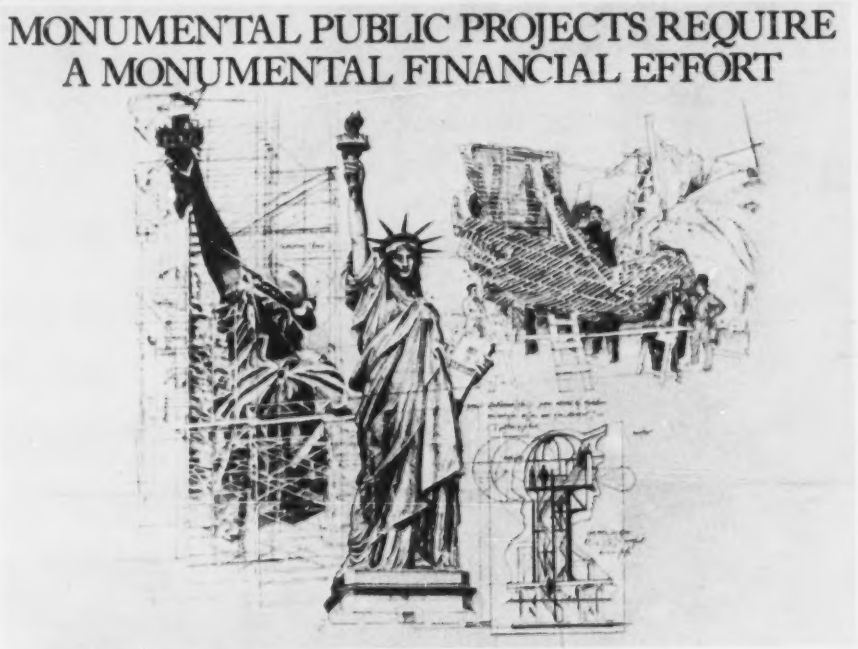

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